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BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554

FCC 96-93

In the Matter of	)	
	)	
Federal-State Joint Board on	)	CC Docket No. 96-45
Universal Service	)	

COMMENTS OF KENTUCKY PUBLIC SERVICE COMMISSION
REGARDING FEDERAL-STATE JOINT BOARD
UNIVERSAL SERVICE RECOMMENDED DECISION

Submitted By:

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Comes now the Kentucky Public Service Commission ("Kentucky Commission") and for its comments regarding the Federal-State Joint Board Recommended Decision states as follows:

In April 1995, the Kentucky Commission initiated a proceeding to investigate local competition and its effect on universal service, and the potential need for changing non-traffic sensitive access charges.[1] The Kentucky Commission entered an order September 26, 1996 ("Kentucky Order") addressing issues relating to local competition including the preservation of universal service. A copy of this Order is attached hereto and incorporated herein. All determinations regarding universal service are preliminary. They are subject to the Federal Communications Commission's ("FCC") decision on universal service, expected in May 1997, and to conclusions reached in upcoming workshops to be sponsored by this Commission.

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1 Administrative Case No. 355, An Inquiry Into Local Competition, Universal Service, and the Non-Traffic Sensitive Access Rate.

The parties to the Kentucky proceeding will have the opportunity to participate in these workshops and to file comments. The Commission staff will conduct workshops to be scheduled in the first quarter of 1997 to allow comments and to make recommendations to the Kentucky Commission for determinations regarding the definition of universal service, affordable rates, support of rural and high cost areas, support of low income consumers, advanced services for schools, libraries and health care providers, and reasonably comparable rates. These recommendations are due to the Kentucky Commission 90 days after the workshops commence. Kentucky Order at 41.

The most unique aspect of the Kentucky Commission's Universal Service Fund proposal is the incentive to spur rural facilities-based competition. We have tentatively decided to distribute Universal Service Fund dollars to eligible telecommunications carriers based on the number of residential rural customers served by the carrier. Using only the number of rural residential access lines as opposed to all access lines means that the universal service payment per line will be relatively higher than would otherwise be the case. Kentucky Order at 38.

The Kentucky Commission strongly disagrees that intrastate revenue should be included in a new national universal service support mechanism. The Kentucky Commission has tentatively determined that contributions to the Kentucky Universal Service Fund will come from an assessment on the gross intrastate revenues of each carrier. Kentucky Order at 36. To include intrastate revenues in any other support mechanism would result in a double assessment of intrastate revenues. The Kentucky

Commission endorses comments made by Commissioner Ken McClure of Missouri in his separate statement to the Joint Board's recommended decision:

> Section 254(d) states that "every telecommunications carrier that provides interstate telecommunications services" must contribute to preserve and advance universal service. Congress required that these contributions be made on an "equitable and nondiscriminatory basis" and mandated that contributions be provided by telecommunications carriers that provide interstate telecommunications services. When that requirement is read together with Section 254 (f), which contemplates state universal service programs, it is [our] opinion that Congress intended the specific reference to interstate carriers to mean that a distinction should be made for a separate federal support mechanism. Only interstate revenues should be utilized for funding the federal universal service program, allowing intrastate telecommunications revenues to be used for funding the complimentary state universal service programs.

Appropriate universal service support forms the critical cornerstone for the advancement of competition in Kentucky. Each state must have the latitude to develop basic programs to support universal service within its borders.

The Kentucky Commission agrees with the Joint Board recommendations that further analysis of proxy cost models is needed to produce an accurate model to determine universal service support. However, the tentative estimate of the size of the Kentucky intrastate fund is $90 million, consisting of a local exchange company specific non-traffic sensitive revenue requirement, Lifeline assistance and fund administration costs. Kentucky Order at 36 and 51, footnote 119. The Kentucky Commission has serious concerns about the possible size of the federal fund and believes it could impede the delivery of competition's benefits to the end-user.

The Kentucky Commission does not believe that Congress in the Telecommunications Act of 1996 ("the Act") intended to provide universal service support to businesses and, therefore, does not agree that support should be provided for service to a single-connection business line. Support for business lines will necessitate an unreasonably large fund. The Kentucky Commission has tentatively decided to support only the first access line to a residential subscriber. Kentucky Order at 30 and 38.

The Kentucky Information Highway, a state-wide network that is available to state and local governments, offers access to the network for schools, public libraries and public health care facilities at a discounted rate. This, we believe, satisfies the discount requirements in the Act. Kentucky Order at 40 and 41. Further discounts should not be mandated at this time.

The Kentucky Commission agrees with the Joint Board's recommendation regarding the monitoring of rates and non-rate factors to determine norms for low penetration. The Kentucky Commission has outlined factors to be considered in universal service workshops to determine the reasons for low penetration rates. Kentucky Order at 43 and 44. Lifeline assistance is projected to be a major focus of universal service in Kentucky. Kentucky Order at 23 and 24.

Only federal and state cooperation will produce a rational system for universal support which will not endanger consumer benefits.

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing Comments of Kentucky Public Service Commission Regarding Federal-State Joint Board Universal Service Recommended Decision has been served by first-class mail, postage prepaid, on the following this 18th day of December, 1996.

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COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

RECEIVED
DEC 19 1996
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In the Matter of:

AN INQUIRY INTO LOCAL COMPETITION, UNIVERSAL SERVICE, AND THE NON-TRAFFIC SENSITIVE ACCESS RATE	)))	ADMINISTRATIVE CASE NO. 355

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COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

AN INQUIRY INTO LOCAL COMPETITION, UNIVERSAL SERVICE, AND THE NON-TRAFFIC SENSITIVE ACCESS RATE	)))	ADMINISTRATIVE CASE NO. 355

O R D E R

PROCEDURAL BACKGROUND

On April 21, 1995, the Commission initiated this proceeding to determine the viability of local competition and, in that context, to explore ways to preserve and expand universal service goals. This proceeding was initiated also to address the feasibility of reduction or elimination of the non-traffic sensitive revenue requirement as the telecommunications industry moves toward market-based rates. All telecommunication carriers, the Office of the Attorney General ("AG"), and various others are parties to this docket. Replies to the Commission's initial inquiry were received from approximately 25 entities.

On July 22, 1995, the Commission entered a procedural schedule and stated that all replies and comments would be considered prefiled testimony. Additional comments or prefiled testimony were permitted to be filed by February 26, 1996. The Commission ran notices in newspapers of general circulation to inform Kentuckians of their opportunity to comment in writing or at the public hearing.

A public hearing was held March 25 to 29, 1996. Fourteen parties presented a total of 27 witnesses. Parties presenting witnesses were BellSouth Telecommunications, Inc. ("BellSouth"); Cincinnati Bell Telephone Company ("CBT"); GTE South Incorporated ("GTE"); ALLTEL Kentucky, Inc. ("ALLTEL"); TDS Telecom ("TDS"); AT&T Communications of the South Central States ("AT&T"); the Independent Telephone Group ("ITG");[1] MCI Telecommunications Corporation and MCI Metro Access Transmission Services, Inc. ("MCI"); Sprint Communications Company L.P. ("Sprint"); WorldCom, Inc. d/b/a LDDS WorldCom ("LDDS"); American Communication Service of Louisville, Inc. ("ACSI"); BellSouth Cellular Corporation ("BSCC"); Kentucky CATV Association, Inc. ("KCTA"); and the AG. Metro Human Needs Alliance cross-examined witnesses. Briefs were filed May 17, 1996.

In addition to witnesses presenting testimony, public comments were given at the hearing by several persons. Jerome Hicks of Marshall County argued for county-wide toll-free calling on behalf of the Kentucky Master Commissioners Association. John Stephenson of Fort Mitchell, Kentucky, associated with "public education and government access," requested that public rights-of-way and public access to communications be a high priority of this Commission. Gary Higdon of the Louisville

1 The ITG is comprised of Ballard Rural Telephone Cooperative Corporation, Inc., Brandenburg Telephone Company, Inc., Duo County Telephone Cooperative Corporation, Inc., Foothills Rural Telephone Cooperative Corporation, Inc., Harold Telephone Company, Inc., Highland Telephone Cooperative, Inc., Logan Telephone Cooperative, Inc., Mountain Rural Telephone Cooperative, Inc., North Central Telephone Cooperative, Inc., Peoples Rural Telephone Cooperative, South Central Rural Telephone Cooperative, Thacker-Grigsby Telephone Company, Inc., and West Kentucky Rural Telephone Cooperative.

Apartment Association and Todd Strecker of Lexington On-Line asked that the Commission maintain access to communication facilities and advanced services. Laurel True of the Kentucky Association of Retired Persons spoke of the need for universal telephone service for low-income Kentuckians. Telemedicine issues were addressed by Dr. Peter Bosomworth, former Chancellor at the University of Kentucky Medical Center, and David Bolt, working in network development for St. Claire Medical Center in Morehead. Mr. Bolt also presented comments of Dr. Claire Louise Caudill on developing advanced technologies for rural health care. Dr. Bosomworth touted the benefits of distance insensitive pricing on the Kentucky Information Highway. Lastly, Joe Kelly, Chairman of the Kentucky Board of Education, spoke on behalf of the Kentucky Department of Education and the Kentucky Educational Technology Systems ("KETS"). He stated that voice, video, and data technology is being deployed to all public schools, including schools in low-income counties. Mr. Kelly argued for advanced, quality services at affordable rates and for universal service and resource sharing.

On February 8, 1996, the Telecommunications Act of 1996 ("the 1996 Act") became law.[2] The 1996 Act said that local competition in telecommunication markets is in the public interest. With that determination having been made by passage of the 1996 Act, the focus of this proceeding changed from determining the feasibility of local competition to implementing it. Since the passage of the 1996 Act, the Federal Communications Commission ("FCC") has issued several notices of proposed rulemaking to implement the 1996 Act. One involves unbundling of network elements,

[2] The 1996 Act is codified at 47 U.S.C. § 151 et. seq.

interconnection, and resale (CC Docket No. 96-98) and the other involves universal service (CC Docket No. 96-45). On August 8, 1996, the FCC adopted rules to implement local competition (hereinafter cited as the FCC Order).[3]

Decisions reached in this Order are based on the extensive record in this proceeding. Parties have had ample opportunity to express their views and respond to those of others. The Commission has reviewed the record and given due weight to all evidence. We have looked to the FCC Order for specific guidance, but all findings are rooted in statements and arguments made to this Commission.

We discuss the issues of interconnection and unbundling network elements first, then discuss resale discounts and universal service issues, rural company exemptions, and, finally, implementation of local competition.

INTERCONNECTION AND UNBUNDLING NETWORK ELEMENTS

The 1996 Act and the FCC Order place important emphasis on the role of negotiated agreements for the interconnection of telecommunications carriers' networks. Various obligations are assigned to all local exchange carriers ("LECs") and additional obligations are assigned to incumbent LECs ("ILECs"). All LECs are to allow resale of telecommunications services, provide number portability, provide dialing parity, allow access to rights-of-way, and establish reciprocal compensation for transport and termination of traffic. ILECs are to negotiate interconnection agreements, provide

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3 Implementation of the Local Competition Provisions in the Telecommunications Act of 1996 (CC Docket No. 96-98) and Interconnection Between Local Exchange Carriers and Commercial Mobile Radio Service Providers (CC Docket No. 95-185) FCC 96-325, First Report and Order, released August 8, 1996.

interconnection, provide unbundled access to network elements, and provide resale without discrimination.[4] However, negotiated arrangements for interconnection are intended to take precedence over any generally established standards or any prescribed regulations. The Commission embraces this concept and finds that implementing specific rules for interconnection at the state level, at the outset, is not necessary and may only jeopardize the balance necessary for fully negotiated agreements.

The 1996 Act authorizes the Commission to resolve any disputes through compulsory arbitration procedures. The Commission's decisions will be binding and may apply to all existing, as well as subsequent, agreements. This authority and the general guidelines of the 1996 Act empower the Commission to implement its policy on a case-by-case basis as petitions for arbitration are filed. The availability of resale services and unbundled elements is basic for alternative LECs ("ALECs") initially to provide local service. However, the Commission considers facilities-based competition essential to a truly competitive telecommunications market. Therefore, the Commission intends to encourage ALECs ultimately to invest in their own facilities rather than to rely solely on the ILECs' networks. In addition, the Commission will ensure that adequate incentives exist to promote investment by the ILECs for the continued quality of telecommunications services.

The Commission's review of negotiated interconnection agreements is somewhat limited in that an agreement may be rejected only if it discriminates against a telecommunications carrier not a party to the agreement or if the agreement is not

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[4] 47 U.S.C. § 251.

consistent with the public interest, convenience, and necessity.[5] In contrast, the review of disputed issues during arbitration is extended to include consideration of compliance with the interconnection requirements and pricing standards of the 1996 Act and subsequent FCC regulations.[6] This is evidence, again, of the 1996 Act's incentive for negotiated interconnection agreements in place of prescribed rules.

With regard to interconnection issues, the Commission finds that the framework created by the 1996 Act is sufficient for introducing competition in the local exchange and exchange access markets. The Commission intends fully to review areas of dispute through the arbitration process and will base its decisions on the information gathered through that process.

The Commission concludes that interconnection and unbundling workshops are not necessary at this time. However, the Commission intends to review interconnection related issues that may arise in the future, through complaints, upon motions of affected parties, or upon the Commission's own motion.

<u>RESALE</u>

The 1996 Act charged state commissions with the duty of determining the rates at which telecommunications services will be available for resale. Specifically, Section 252(d)(3) of the 1996 Act states:

> For the purposes of Section 251(c)(4), a State commission shall determine wholesale rates on the basis of retail rates charged to subscribers for the telecommunications service

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5 Id. at § 252(e)(2).

6 Id. at § 252(b).

requested, excluding the portion thereof attributable to any marketing, billing, collection, and other costs that will be avoided by the local exchange carrier.

During this proceeding, the Commission has investigated the rates at which telecommunications services will be available for resale and has reviewed the FCC Order.

Duty to Offer for Resale

Section 251(c)(4)(A) imposes a duty on ILECs "to offer for resale at wholesale rates any telecommunications service that the carrier provides at retail to subscribers who are not telecommunications carriers."

AT&T believes that all current and future retail offerings of the ILEC should be available for resale, including promotional and trial offerings.[7] Included in AT&T's list are local exchange and vertical services, intrastate toll, private line, and centrex services, among others. AT&T also believes that operator services should be unbundled from the local service offering[8] and that the ILEC should provide basic white page and basic yellow page listings for reseller's customers at no cost to the reseller or the reseller's customers.[9]

The FCC concludes that an ILEC must establish a wholesale rate for each retail service that: (1) meets the statutory definition of a "telecommunications service"; and

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7 Testimony of Mike Guedel for AT&T at 9 - 10.

8 Id. at 33.

9 Id. at 34 - 35.

(2) is provided at retail to subscribers who are not "telecommunications carriers."[10] The FCC has not prescribed a minimum list of services to be resold, choosing instead to leave to the discretion of the state commissions, ILECs, and resellers to determine the services that an ILEC must provide at wholesale rates by examining an ILEC's retail tariff.[11] The FCC has, however, precluded the resale of exchange access services[12] and has concluded that ILECs are not required to make available service to independent public payphone providers at wholesale rates.[13] Finally, the FCC pointed out that the resale obligations do not impose on an ILEC the obligation to disaggregate a retail service into more discrete retail services.[14]

The Commission will not prescribe a minimum list of services subject to resale. Instead, we leave the determination of such services to the negotiation process set forth in Section 251 of the 1996 Act. Only at such time as parties cannot reach agreement through negotiations will the Commission consider the issue of resale services subject to the schedule set forth in Section 252(e)(4). The Commission will not require ILECs to unbundle services in their retail tariffs for resale. The FCC declined to impose on ILECs the obligation to disaggregate a retail service into more discrete retail services; therefore, AT&T's request to unbundle access to operator services from the local service

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10 FCC Order at paragraph 871.

11 Id. at paragraph 872.

12 Id. at paragraph 873.

13 Id. at paragraph 877.

14 Id.

is denied.[15] AT&T additionally requested several elements to be included in the ILECs' resale tariff. The Commission will consider each ILEC's resale tariff on an individual basis and follow the requirements of the FCC Order. ILECs will be required to provide white page listings for resellers, but the Commission will not require the inclusion of yellow page listings because these listings are the product of a contractual relationship between ILECs and directory publishing companies.

Wholesale Pricing

BellSouth presented in its testimony the results of an internal cost study showing costs it would avoid by making services available for resale in Kentucky. BellSouth determined the appropriate discount would be 9 percent for residential services and 8 percent for business services.[16] BellSouth was the only company to provide a cost study quantifying costs and supporting a wholesale discount.

MCI agrees with the language of the 1996 Act and has not suggested any percentage of discount. Nevertheless, it warned the Commission that the percentages presented by BellSouth should be scrutinized for understatements of avoided costs that would give an advantage to the incumbent carrier.[17]

AT&T also testified regarding a wholesale discount, urging that a discount ranging from 36 percent to 50 percent be applied to all services for resale.[18] AT&T bases these

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[15] Id.

[16] Rebuttal Testimony of Frank R. Kolb, Jr. for BellSouth at 2.

[17] MCI Brief at 28.

[18] Testimony of Mike Guedel for AT&T at 23 - 26.

percentages on its analysis of other jurisdictions, upon which it has concluded that a LEC could save 26 percent or more in providing services at the wholesale level.[19] AT&T further asserts that as a reseller it will face operational inefficiencies for which an additional discount of 10 percent should be applied. These figures, contends AT&T, produce a minimum discount of 36 percent.[20] AT&T further proposes a 50 percent discount justified on the basis that the ILEC will have tremendous market advantages and power and, without a significant discount, competitors will not risk entering the market.[21]

KCTA's position is that resale discounts should be established following the literal wording of the 1996 Act, based on the marketing, billing, collection, and other costs that will be avoided by the local exchange carrier.[22] It feels that the Commission should not mandate a discount based on hypothetically "avoidable" costs.[23] The KCTA also states that an artificially high resale discount rate to jump start competition or as a means to force LECs to submit accurate and verifiable cost information is not consistent with the 1996 Act and could have the unintended effect of forestalling facilities-based

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19 Id. at 24.

20 Id. at 26.

21 Id. at 24.

22 KCTA Brief at 24.

23 Id.

competition.[24] The KCTA believes that most resale issues, especially pricing issues, must be resolved through further Commission proceedings.[25]

CBT advocates that the optimal resale discount for resold services should be based on the existing downstream market price and the net costs that will be avoided, which includes the net of the wholesale costs added and the retail costs avoided.[26] CBT opposes applying large discounts to retail rates to determine wholesale rates because it believes that in the long run the market will not benefit. In fact, CBT contends that large discounts would deter others from deploying new facilities.[27]

The AG advocates a 25 percent wholesale discount based on data previously presented to the California Public Utilities Commission which suggests that avoided costs approximate 25 percent of the retail rate.[28] The AG, however, acknowledges that the 1996 Act requires wholesale rates to be discounted from retail rates and the maximum rate to be the retail rate less avoided retail related costs.[29]

The FCC Order has established national rules to determine the statutory pricing standard within which state commissions shall determine (1) the marketing, billing, collection, and other costs that will be avoided by the ILECs when they provide services

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24 Id. at 25.

25 Id.

26 Testimony of Dr. Richard D. Emmerson for CBT at 93.

27 CBT Brief at 9-10.

28 Testimony of Dr. Marvin H. Kahn for the AG at 21.

29 Id.

at wholesale; and (2) the portion of the retail prices for those services that are attributable to the avoided costs. The first and preferred method is to identify and calculate avoided costs based on avoided cost studies. The second method allows states to select, on an interim basis, a discount rate from within a default range of discount rates adopted by the FCC.[30]

The statutory pricing standard for wholesale rates requires state commissions to identify what marketing, billing, collection, and other costs will be avoided by ILECs when they provide services at wholesale and calculate the portion of the retail prices for those services attributable to the avoided costs.[31] The FCC requires states to select a wholesale rate between 17 percent and 25 percent below the retail rates if an avoided cost study that satisfies the criteria set forth below does not exist, if a state commission has not completed its review of such avoided cost study, or if a rate established by a state commission does not comply with the criteria.[32]

There has been considerable debate in this proceeding, as well as at the FCC, on whether section 252(d)(3) of the 1996 Act embodies an "avoided" cost standard or an "avoidable" cost standard. The FCC found that "the portion [of the retail rate]. . . attributable to cost that will be avoided" includes all of the costs that the ILEC incurs in maintaining a retail, as opposed to a wholesale, business.[33] Under this "reasonably

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30 FCC Order at paragraph 908.

31 Id.

32 Id. at paragraph 910.

33 Id. at paragraph 911.

avoidable" standard, an avoided cost study must include indirect, or shared, costs as well as direct costs.[34] A portion of contribution, profits, or mark-up may also be considered "attributable to costs that will be avoided" when services are sold wholesale.[35]

An avoided cost study may not calculate avoided costs based on non-cost factor or policy arguments, nor may it make disallowances for reasons not provided in 47 U.S.C. § 252 (d)(3).[36] Therefore, AT&T's proposed 10 percent penalty discount for inferior interfaces is rejected. The avoided cost study methodology must be consistent with the manner in which retail rates have been set.[37] Different rates for service groups or a single rate for all services will be allowed.[38] The Commission recommends a single discount rate for all services in the interim, but, as may be justified by future cost studies, multiple discount rates will be allowed.

Based on the guidelines established in the FCC Order and the record herein, the Commission disregards the wholesale discount rates proposed in this proceeding. Although BellSouth submitted evidence regarding the discount rate, the Commission finds that BellSouth's methodology is too simplistic, has insufficient detail, and does not comply with the FCC's criteria. AT&T's proposed rate was not supported by any

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34 Id. at paragraph 912.

35 Id. at paragraph 913.

36 Id. at paragraph 914.

37 Id. at paragraph 915.

38 Id. at paragraph 916.

evidence and is not in compliance with the 1996 Act. Similarly, the AG did not base his estimate on any specific cost studies. Therefore, the Commission chooses a wholesale discount rate from the default range.[39] At this time, based on the absence of any studies that comply with the FCC guidelines, the wholesale discount rate for both business and residential service will be the same. For all LECs, other than GTE and BellSouth, the discount rate shall be 17 percent, the low end of the proxy range. GTE shall use 18.81 percent and BellSouth shall use 19.20 percent as their respective wholesale rates.[40] These rates were calculated by the FCC using the modified MCI model. They are interim rates and may not be implemented if appropriate and timely Kentucky-specific avoided cost studies are furnished.

The Commission is required by the FCC to initiate separate proceedings for each LEC to determine the wholesale discount within a reasonable time.[41] We will, therefore, require that avoided cost studies be filed by each LEC as soon as available, but not later than 12 months from the date of this Order, unless otherwise ordered by the Commission. Companies exempted pursuant to Section 251(f)(1) should file avoided cost studies within 3 years from the date of this Order, unless otherwise directed by the Commission.

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39 Id. at paragraph 910.

40 Id. at paragraph 930.

41 Id. at paragraph 934.

Conditions and Limitations on Resale

Generally speaking, the potential ALECs supported MCI's position that all of the services provided by ILECs, including discount plans, promotions, and other service options, must be provided at wholesale rates.[42]

The FCC Order recognizes, as does this Commission, that ILECs possess market power and that resale restrictions are presumptively unreasonable. ILECs may, however, rebut this assumption if the restrictions are narrowly defined.[43] The FCC has discussed specific restrictions, including those discussed in the following subsections, for which the presumption of unreasonableness may or may not apply.

Promotions and Discounts. Promotions are temporarily discounted standard service offerings.[44] BellSouth believes that it should not be required to resell promotional, trial, and special package offerings, as these do not represent retail rates.[45] MCI does not agree that the promotional, trial, and special package offerings may be withheld from resale.[46] The FCC found that the language of the 1996 Act provided no basis for creating a general exemption from the wholesale requirement for all promotional or discount service offerings of ILECs. The FCC also stated, however, that promotional prices offered for a period of 90 or fewer days need not be offered at

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42 MCI Brief at 26.

43 FCC Order at paragraph 939.

44 Id. at paragraph 948.

45 Rebuttal Testimony of Robert C. Scheye for BellSouth at 21.

46 MCI Brief at 27.